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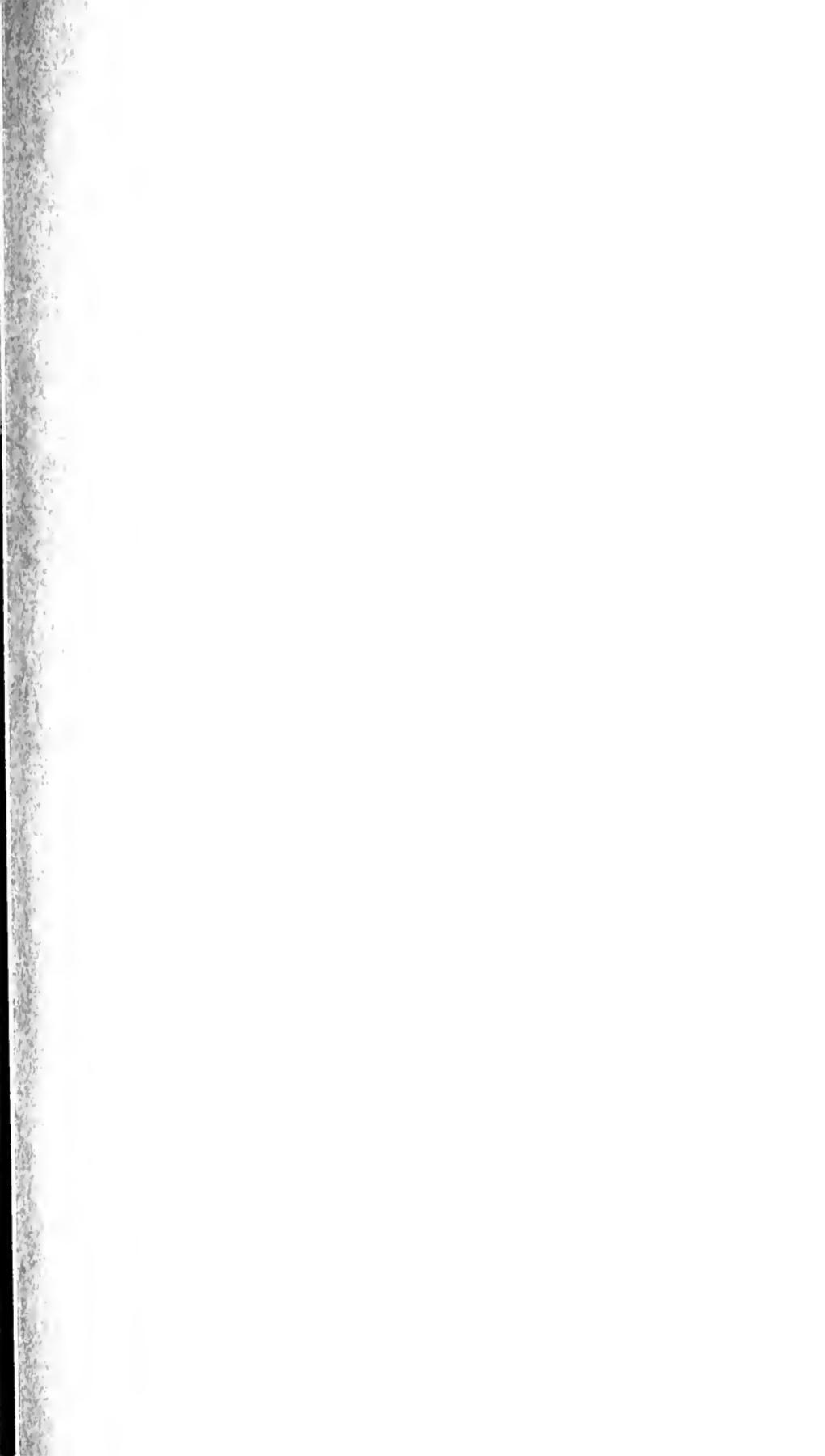


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Loyd.
(Lord Overstone)

On

State of the Currency

1837



FURTHER REFLECTIONS

ON THE

STATE OF THE CURRENCY

AND THE ACTION

OF THE

Bank of England.

BY

SAMUEL JONES LOYD, Esq.

LONDON:

PELHAM RICHARDSON, 23, CORNHILL.

1837.

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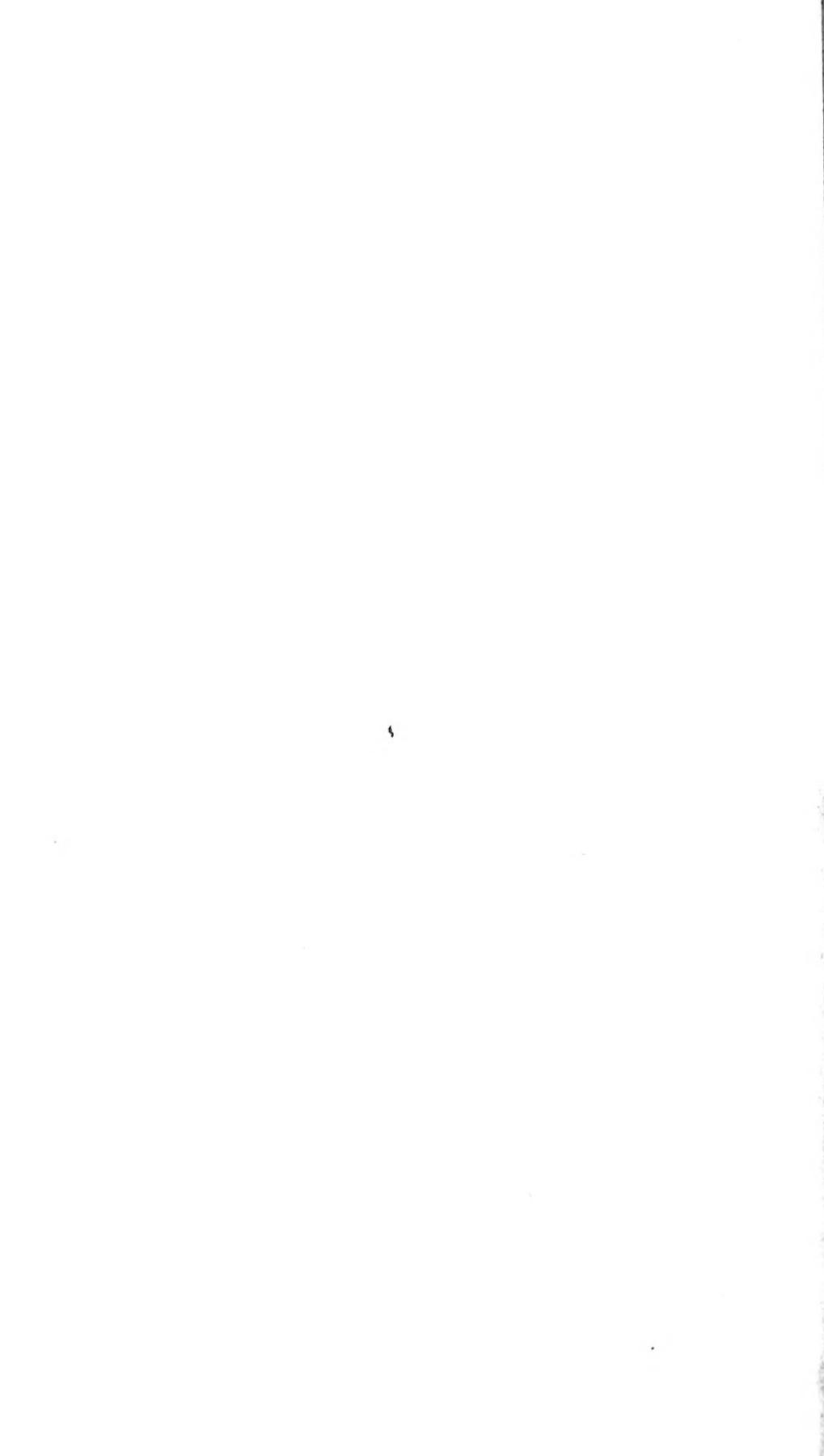
NOT quarrelling—but quietly endeavouring, without ostentation or fear, to resolve by reason, subjects which have hitherto been in possession of “common belief.”

IT is the duty of every one to serve the public in such way for which he is best fitted, how slender soever his ability may be; and this is the only way wherein I have any chance of making myself useful.—*Tucker's Light of Nature.*

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FURTHER REFLECTIONS,

ETC. ETC.

I. IN the month of February last, the writer of the following pages ventured to submit to the public a few remarks upon the state of our monetary affairs, and the conduct of the Bank of England in the management of the currency. The peculiar character of the events then in progress seemed calculated to draw more than usual attention to discussions of that nature, and in adverting to them he endeavoured not only to lay before the public a correct view of the position in which we then stood, but also to derive from passing events some instruction as to the general principles upon which the management of the circulating medium ought to be regulated. Another year has nearly elapsed, and during this period a great change, as might

have been anticipated with perfect confidence, has . taken place in the state of the trading world, and also in the condition in which the Bank of England stands in regard to the regulation of the currency. In the nature of this change and in the circumstances which accompany it, when carefully examined, the writer thinks that a striking confirmation is to be found of the views which he ventured to develop, and that the same events are also pregnant with warnings as to the future which it will be dangerous to neglect.

Under this impression he has again taken the pen in hand ; the position in which he is placed, and the pursuits in which he is at present engaged, necessarily fix his attention with steadiness and constancy upon the fluctuations of the currency, and lead him to watch the mutual connection and inter-dependence of these with the fearful oscillations of our commercial condition. To excite an adequate interest upon this important subject ; to draw public attention with sufficient seriousness to questions of the utmost importance to the steady and equable progress of commercial welfare ; and to invite to the examination of recent events minds of sufficient vigour and sa-

gacity to draw from them the latent lessons of warning and instruction which they contain, is the desire by which he is actuated ; and as Ulysses laid claim to some share of the military honours of Achilles, because he had first detected the symptoms of warlike disposition in the unsuspected hero, and been the means of sending him to deeds of arms ; so would the writer humbly hope that he may succeed in awakening the interest of those who are competent to the investigation of so important a subject, and that he may derive some credit from the useful results of their inquiries.

II. In February, 1837, the circumstances in which the commercial world was then placed were of the most peculiar and critical kind ; we had arrived at the termination of a prolonged period of prosperity ; the excitement and the confidence attending it had reached their utmost point ; the symptoms of an approaching collapse were obvious ; all parties saw them ; all were conscious of their unequivocal character, and a general course of preparation for the approaching change, checked only by occasional dalliance with vague and unsubstantial hopes, had commenced. All traders had become desirous of lessening their stocks on hand,

and of contracting their engagements ; the country issuers had begun effectually to restrict their accommodation ; and all other dealers in money were necessarily compelled to follow in the same course.

The natural effect of this was a general diminution of confidence ; and a state of embarrassment more or less intense on the part of all concerns which were essentially in an unsound state, or whose operations during the late excitement had been unduly expanded.

The situation of the Bank of England at this period was critical and difficult in the highest degree. The first indication of the approaching crisis, not perhaps at the time sufficiently attended to, had been a change in the state of the exchanges ; a heavy drain upon the gold of the Bank had taken place ; her treasure had suffered a continuous and alarming diminution ; and the urgent necessity on that account of a corresponding contraction of her issues was very generally acknowledged. But to effect this was found impracticable ;—the demands for assistance to concerns brought into a state of temporary embarrassment ; the calls of commerce for support during a

period of pressure ; the necessity of preventing, if possible, any convulsion amongst the country issuers, lest the alarm thus produced should cause an internal drain upon the treasure of the Bank simultaneously with the external drain, through the exchanges, under which she was already suffering ; —these considerations, deriving additional weight from the concurrence and sympathy which they met with on the part of a large portion of the public, proved to be irresistible ; and the consequence was that at the period in question the Bank, in rendering her account to the public, appeared in this anomalous and alarming condition :—Her treasure reduced to an unusually low amount, whilst her circulation was undiminished ;—The aggregate amount of securities held by her unusually high, whilst it was notorious that the most realisable class of those securities had been parted with, and that, in lieu of them, in her efforts to meet the demands above alluded to, she had loaded herself with securities of a very different character.

This was the state in which matters stood about the commencement of 1837. It was generally felt by the public to be one calculated to give rise to much

anxiety and apprehension, and to the writer it certainly appeared to be undeniable that the currency of the country was at that time in an unsafe condition ; and that the Bank of England was in a position in which, as manager of the currency, she ought never to be placed.

III. In the reflections which he was led to publish upon the subject at that time, he endeavoured to draw the public attention to the following points.

First. The essential difference between a Bank of Issue and a Bank of Deposit and Discount ; and the incompatibility of their respective functions.

Second. The practical illustration of that difference and incompatibility afforded by the proceedings of the Bank during the preceding months, and also the serious nature of the consequences sure to result from such an incongruous union of functions, as shown in her then alarming situation.

Third. The necessity of adopting some means for separating the management of the currency from all ordinary banking affairs, with the view of enabling the public clearly to understand the proceedings of the body entrusted with the regulation of the currency, and at the same time of protecting

that body from unreasonable expectations and demands, by the pressure of which it must inevitably be diverted from the true line of its duty.

These views were then supported by arguments derived from circumstances as they had occurred up to that period. It would be improper to trouble the reader with a repetition of them, and they are now referred to only as introductory to the further confirmation of the same views which may be derived from the subsequent occurrences of the last year.

IV. Since the beginning of 1837, the circle of commercial progress in which we were then far advanced has been completed—the apprehended convulsion has taken place—embarrassment and insolvency to a considerable extent have occurred—the former excitement has been succeeded by present prostration—prices have fallen—all trading transactions have been materially contracted—and we are now in a state of calm quiescence,—conscious of our present security, but too much occupied in repairing the injuries which we have sustained, and too strongly impressed with the vivid remembrance of the dangers we have so recently escaped, to allow as yet our present sense of safety to en-

gender new projects of enterprise and speculation.

Such is the present condition of the trading community. But what during the past year has been the progress, and what is now the existing position of the Bank of England? In what way has she regulated the amount of her issues during this period, and how do they now stand?

It will be recollect that during the period when the exchanges were against us, and gold was going out of the country, the complaint against the Bank was that her issues, which under such circumstances ought to be diminishing, were in fact increasing; and this increase was pretty clearly traced as the necessary consequence of demands arising out of the union of banking functions with the management of the currency.

We have now to examine her proceedings under opposite circumstances: the change already described in the state of trading operations has brought about its natural and legitimate effect, *i.e.* change in the state of the exchanges; gold has for some time been flowing into the country in a steady and powerful stream; and the treasure of the Bank has been largely increased. Under these

circumstances it is clear that the circulation ought to undergo a corresponding increase. Had it been metallic, the influx of gold which has taken place would have been so much actual increase of the circulating medium; but the currency being in paper, the increase which would in a metallic currency have been effected by the actual addition of the gold imported, ought to be equally effected by an equivalent issue of notes. What, however, is the real state of the case?

That we may be enabled to take a complete view of the action of the Bank upon the amount of the currency during the period both of a favourable and an unfavourable state of the exchanges, a table of her monthly returns, from June 1836 to the present time, is here given.

BANK OF ENGLAND.

1836.	Circulation.	Deposit.	Bullion.	Securities.
June 28....	£ 17,899,000	£ 13,810,000	£ 7,362,000	£ 27,153,000
July 26....	17,940,000	14,495,000	6,926,000	28,315,000
August 23..	18,061,000	14,796,000	6,325,000	29,345,000
Sept. 20 ..	18,147,000	14,118,000	5,719,000	29,406,000
Oct. 18	17,936,000	13,324,000	5,257,000	28,845,000
Nov. 15 ..	17,543,000	12,682,000	4,933,000	28,134,000
Dec. 13....	17,361,000	13,330,000	4,545,000	28,971,000
1837.				
Jan. 10....	17,422,000	14,354,000	4,287,000	30,365,000
Feb. 7	17,868,000	14,230,000	4,032,000	31,085,000
March 7 ..	18,178,000	13,260,000	4,048,000	30,579,000
April 4	18,432,000	11,192,000	4,071,000	28,843,000
May 2	18,480,000	10,472,000	4,190,000	28,017,000
May 30....	18,419,000	10,422,000	4,423,000	27,572,000
June 27 ..	18,202,000	10,424,000	4,750,000	26,932,000
July 25....	18,261,000	10,672,000	5,226,000	26,727,000
August 22..	18,462,000	11,005,000	5,754,000	26,717,000
Sept. 19 ..	18,814,000	11,093,000	6,303,000	26,605,000
Oct. 17....	18,716,000	10,501,000	6,856,000	25,316,000
Nov. 14 ..	18,344,000	10,242,000	7,432,000	23,985,000
Dec. 14 ..	17,998,000	10,195,000	8,172,000	22,727,000

Upon casting the eye over this table there are two considerations which cannot fail to arrest our attention.

1. The principle upon which the Bank proposed to guide its proceedings in the management of the currency was that of keeping the amount of its securities fixed; and the present periodical publication of its accounts in the Gazette was adopted principally for the purpose of enabling the public to understand its proceedings, and to satisfy themselves that they are conducted in obedience to the rules laid down. By these accounts, however, it appears that the securities, instead of being kept at a fixed amount, have fluctuated to a very great extent. Either, then, the Bank has failed to adhere to its own rule, or the accounts as published are wholly insufficient to afford the public a just view of its action.

The apparent fluctuation in the amount of securities during the year 1836 was explained by a reference to some peculiar and unusual transactions, which, it was contended, ought to be struck out of the account, and this being done, the amount of securities, it was said, would approach to steadiness. Is any similar explanation to be

afforded of the present remarkable diminution in the amount of the securities? If so, of what value is the published column of the securities for the information or satisfaction of the public? If not, the rule laid down by the Bank for its own guidance is obviously abandoned.

Which of these suppositions is the correct one can be decided positively by those only who have means of access to other accounts of the Bank than those which are submitted to the public. But there are grounds upon which, though it may be presumptuous to decide, we may still surmise with some confidence that the fluctuation in question is not altogether the effect of a peculiar and distinct transaction, but that it arises out of the ordinary action of the Bank upon the currency.

In the first place, it is to be observed that the increase in the amount of securities took place concomitantly with an equally remarkable diminution of the amount of bullion, and during a period when commercial pressure and embarrassment was gradually approaching after a state of high commercial excitement; and that the amount of securities was at the maximum at the very

moment when the amount of bullion was at the minimum. (See the table for the year 1836) On the other hand, we find the securities regularly diminishing as the bullion as regularly increases until we come to the converse of the former state, and find the highest amount of bullion and lowest amount of securities coincident in point of time. This latter process, too, has been going on principally during the gradual removal of commercial pressure and the return to quiescence.

In the second place, we see, by the table, that the diminution of securities during 1837, though rapid and large, has been regular and equable in its progress, thus exhibiting the strongest presumptive evidence that it is an effect proceeding from some cause which has been in continuous and uninterrupted action.

And in the third place, we know that an important portion of the securities held by the Bank during the year 1836 consisted of those which she received in her various efforts to support public credit—such as increased extent of discounts, aid rendered to concerns tottering under the pressure of overgrown transactions, and means provided to enable others actually in a state

of suspension to discharge at once their debts to the public. It is hardly possible to doubt that during the year 1837 the advances of the Bank of this nature have been in a course of repayment, and must at this moment be very much less than they were twelve months since.

These considerations would lead us to conclude, without much hesitation, that the great diminution in the amount of securities held by the Bank is the inevitable result of her banking operations during the period of tranquillity which succeeds a commercial convulsion.

But it is not necessary to dwell longer on this branch of the subject. Steadiness in the amount of the securities has been held out as a guiding principle with the Bank. “The Bank holds a fixed amount of securities, notwithstanding the altered amount of deposits, except in particular and extraordinary circumstances,” (Palmer’s Reply, p. 7,) and it was therefore impossible not to remark upon the discrepancy between this rule and the column of securities in the annexed table. We are not, however, ourselves disposed to lay too much stress upon this rule, inasmuch as we conceive that steadiness in the amount of the securities is a prin-

ciple applicable to the management of currency only, and wholly inapplicable to the conduct of banking operations in any form. When it is applied to the combined operations of the Bank in her double capacity, we conceive that it is impracticable, and the published accounts seem to verify this opinion.

2. We will, therefore, pass on to the next and far more important consideration to which an examination of the foregoing table will necessarily draw our attention; that of the relation between the fluctuations in the amount of circulation and those in the amount of bullion.

It will be observed that during the year 1837 the amount of bullion has been steadily increasing, being at the end of the year double the amount at which it stood at the beginning of it. Now it is clear that had the circulation been metallic, it would, during this time, have increased to the extent to which the bullion in the Bank has been augmented, *i.e.* nearly four millions, and, consequently, if the paper-circulation be made to vary as a metallic circulation would have varied, it will during this time have undergone an increase of nearly four millions. But upon turning to the

column of Circulation, we find that it stands now at nearly the same amount at which it stood when the bullion was at the lowest point; and that it has actually undergone a large reduction during the last three months concomitantly with a large increase of bullion.

But the Bank laid down other rules than this for its guidance, and it has been contended that the Legislature and the public gave an implied acquiescence in those rules. Let us, then, try the proceedings of the Bank by them.

One of these was steadiness in the amount of the securities, upon which we have already made all the remarks which it seems to require.

The other rule was, that the fluctuations in the amount of bullion should be met by a corresponding fluctuation in the aggregate amount of circulation and deposits. Against the soundness of this rule we urged, on a former occasion, what appeared to us to be conclusive objections; but if the conduct of the Bank during the past year be tried by this test, the condemnation of it will even be more conclusive than when tried by the rule for which we have contended.

In March 1837 it was maintained in Mr. Palmer's

Reply (p. 7.) "that the Bank has acted up to the principle declared in the year 1832, before the Committee upon the Bank Charter;" that principle being that the joint liabilities of notes and deposits were to vary as the amount of bullion. Let us, therefore, compare the account rendered by the Bank at that time with the account last published by her.

March 7.

Circulation	£18,178,000	Bullion	£4,048,000
Deposits	13,260,000		
	—————		
Joint Liabilities ..	£31,438,000		
	—————		

December 14.

Circulation	£17,998,000	Bullion	£8,172,000
Deposits	10,196,000		
	—————		
	£28,194,000		
	—————		

By this statement it appears that the bullion has increased £4,124,000, whilst during the same period the joint liabilities have diminished, not increased, £3,244,000. Therefore it is clear that the joint liabilities have not varied as the bullion has varied, and consequently the rule laid down by the Bank has not been observed.

It is equally clear by the table that the circulation has not varied as the bullion, and therefore the rule contended for by us has not been observed.

Let us now contrast the amount of securities at these two periods.

March 7,	Securities	£30,579,000
December 14,	Ditto	22,727,000
	Decrease of Securities..	£7,852,000

Here we find a very large diminution in the amount of securities ; what amount the Bank will contend ought to be struck out of the account as arising out of deposits of an unusual and extraordinary character it is impossible for us to say ; but it is hardly possible to believe that so great a difference in the amount of securities can be satisfactorily explained on such grounds.

To enable us, moreover, to come to a correct estimate of our actual situation at the present moment, it is necessary to remark that the statements here commented upon merely show the average condition of the Bank during the three preceding months ; and there is good reason to apprehend that the discrepancies apparent upon the average statement given to the public would be

found to be still more wide and striking, if we had before us an account of the bullion, circulation, &c., as they now actually stand. Indeed it is in the very nature of an average statement that it does not show the extreme points either of elevation or depression, but only the mean point attained during the three months for which the average is calculated. We may therefore conclude almost without the possibility of error, that the circulation and the securities, which have been in a course of diminution during the last three months, are at this moment much below the amount given in the last average return; and that the bullion is much higher than it appears to be by the same statement. Upon the same principle we may take it for certain that the actual amount of bullion at the beginning of the year, when by the average return it appears at the minimum, was in fact much lower than that statement shows, and the securities at the same period much higher. A due attention to these considerations is necessary to enable us to form a correct estimate of the full extent to which the fluctuations under discussion have really gone; though it is difficult to believe that there is not some great error in statements which lead to conclusions so extraordinary.

The Bank holds out to the public, as the best practicable security for the due management of the currency, steadiness in the amount of the securities held by it, and a variation in the aggregate amount of circulation and deposits corresponding with the variation in the amount of bullion.

A strict adherence to sound principle requires a variation in the amount of circulation alone corresponding to the variation in the amount of bullion.

For the purpose of satisfying the public that those rules are sufficiently attended to, the Bank is required to make a periodical publication of her accounts ; and by these it appears that during the last year the securities have diminished from thirty-one millions to less than twenty-three millions ; the aggregate of circulation and deposits shews a decrease of nearly four millions ; whilst in the same period the bullion has risen from four millions to eight millions.

In the face of these facts, is it not idle to talk of rules, or to refer to tables of published accounts, for our satisfaction ? It must surely be admitted that the regulation of the currency is in no degree subject to the stern restraint of principle ; and, indeed, we cannot well avoid the conclusion that

the power of controlling it has passed out of the hands of the Bank.

VI. But whence arises this state of things, which we may, without incurring the charge of exaggeration, describe as extraordinary and alarming? To what causes are we to attribute it? It is easy to throw out, as is too often done, vague and ambiguous imputations against the Directors of the Bank, charging them at one time with dishonest purposes as regards the public, arising from a desire to promote their private interests either individual or those of their proprietors; at another time imputing to them a degree of blindness and ignorance which is utterly incredible. The cause of truth is little promoted by such unreasonable and absurd imputations. The Bank Directors cannot fail to perceive the considerations which we have pointed out; neither can any reasonable person doubt that they both know what their duty requires of them and are anxious to perform it. Indeed the conduct of a public body such as the Bank of England cannot, we conceive, be at any time much in arrear or much in advance of the existing state of public intelligence. In the one case it will be impelled by censure, in the other it will be obstructed by prejudice. It is not with the

view of countenancing in the slightest degree any imputation upon the intelligence or the integrity of those who direct the operations of the Bank, that we have entered upon this discussion ; but for the purpose of drawing the public attention to the almost inextricable difficulties in which they appear to be involved by the peculiar position in which the Bank is placed, and the mixed duties which she undertakes to perform.

The difficulty in which the Bank is now placed as Manager of the Currency, and the present improper state of the circulation, we believe to arise principally from the unfortunate union in the same body of banking functions and the management of the circulation ; and we further fear that the most formidable impediment to the adoption, in the present emergency, of proper measures by the Bank, arises from erroneous views and unreasonable expectations on the part of a large portion of the public.

It will be remembered that during the year 1836 the Bank was urgently called upon to support public credit, and in consideration of her position as a great Bank of Deposit and Discount, and of the strong tone of public expectation on the subject, it was deemed by those who managed her affairs that

this call could not be refused. Hence arose an increase of her circulation whilst her bullion was rapidly diminishing, and an exchange of convertible securities for others which were of a different description. As Manager of the Circulation this was an unwarrantable transaction on her part; it placed her, both as regarded the amount of her circulation and the nature of her securities, in an improper position—it was necessitated by her character of a Bank of Deposit and Discount.

But the evil did not terminate here. In the following year (1837), after the convulsion had taken place, the position of the Bank and her duties as Manager of the Currency became altered, the exchanges turned in our favour, and the bullion in the Bank began steadily to increase. Against this increased amount of bullion there ought of course to be issued a corresponding amount of notes; and this would necessarily take place did the Bank act solely in her capacity of Manager of the Currency. But the very circumstances which turned the exchanges and thus increased the bullion have tended also to relieve those concerns which in the previous year were obliged to resort to the Bank for support, and the securities taken from them now come into a course of rapid discharge. To this the Bank

cannot object, and the consequence is that her securities are inevitably reduced at a time when circumstances render it peculiarly requisite that their amount should be kept up; and the increase of her circulation effected by the issue of notes against the bullion brought in to her is more than compensated by the payments made to her in redemption of the securities in question. Hence a diminishing amount of circulation with an increasing amount of bullion, and all the recognized rules for the management of the currency unavoidably violated.

Such are the consequences of uniting the functions of Banking with the management of the Currency; the steady and unbending course which ought to be pursued with respect to the latter is necessarily interrupted by any connexion with the former. It compels an increase of the circulation and a change from convertible to inconvertible securities at a time when the state of the exchanges requires a diminution of the circulation, and renders it expedient that the Manager of the Currency should have all its resources at its free disposal. And again, when the altered state of the exchanges requires and naturally tends to bring about an increase of the circulation, it thwarts that ten-

dency, renders it impracticable to maintain the proper amount of circulation, and thus brings the Bank and the circulation into their present anomalous and unsatisfactory position.

VII. The proper remedy for the existing difficulty would be a determined action on the part of the Bank for the purpose of keeping up the amount of its securities, and making the circulation vary at least in some proportion relative to the increase of bullion. Was the Bank limited to the duty of managing the currency, or was that business kept totally distinct and separate from her other functions, it seems hardly possible to doubt that some such measure would ere this have been resorted to. But in her banking capacity she is subjected to the strong action of opinion on the part of that portion of the public which is engaged in trading and mercantile operations. By this influence she was compelled, as we have seen, to increase her issues at an improper moment, and from the apprehension of the same influence she is now deterred from effecting that increase which a regard to sound principle would require.

Had she refused the aid required from her in 1836, we are well aware of the severe censure with which she would have been visited by a large

portion of the trading community; and had she at the present moment done that which a proper regard to principle requires from her, we are equally aware of the opposite attacks to which she would be exposed. A desire to augment her private profits at the sacrifice of the public interests, and a disposition to foster speculation by augmenting an already redundant currency ; an attempt to raise the price of public securities, and to drive capital out of the country by lowering the value of money, already too cheap ;—these and other imputations of a similar nature would be freely levelled against her; and it is another unfortunate consequence resulting from the union of her banking with her monetary functions, that it both gives to the imputations a degree of plausibility which they would not otherwise possess, and also renders the Bank more susceptible of their influence.

Still, however, although these considerations may explain the nature of the difficulty in which the Bank is now placed, they cannot be admitted as a justification on her part for the abandonment of all regard to rule or principle in the management of the currency. If any portion of the public, either through want of a sufficient examination of the principles of the subject, or blinded by a mistaken

view of its own interests, is induced to adopt erroneous and pernicious opinions, it is hardly necessary to observe that the Manager of the Currency is imperatively bound to meet such prejudices by an uncompromising adherence to sound principles, and by every proper effort to render the nature of her proceedings and the reasons for them intelligible to the public. With this view an occasional *compte rendu* on the part of the Bank, stating with fulness and perspicuity the course she was pursuing and the reasons by which she was guided, might be of essential service. In proportion as the principles of currency are better understood by the public, will the Bank be enabled to discharge its duties with greater facility ; and it may be well for those who manage that establishment to consider how far the deficient intelligence and consequent prejudices on the part of the public, which at present obstruct their course, are justly attributable to that rigid reserve and total abstinence from all statement and explanation which so long characterised the proceedings of the Bank.

VIII. Do you then—it will be urged by some persons—really maintain that the Bank ought to increase the amount of the circulation under present circumstances ? Is it right to lower the value

of money, already too cheap? Is it fitting that the Bank should resort to forced measures for putting out her notes, when the cessation of the legitimate demand for them affords a sure indication that the wants of commerce are adequately supplied? If the Bank lowers the rate of discount, and increases her issues when money is at this moment a drug in the market, will she not be justly chargeable with voluntarily fostering the spirit of speculation, and encouraging the commencement of another career of excitement and subsequent convulsion? Lastly, Will not the Bank, by adopting this suggestion, inevitably drive capital out of our own country, and force the employment of it in foreign funds, or in supporting the improvement of rival nations?

In stating these objections, we have endeavoured to give not merely the substance, but, as nearly as possible the very form of words in which we meet with them either in the conversation of individuals, or in the organs through which the opinions prevalent on the public mind are usually expressed.

The statement of objections is always more easy and concise than the refutation of them, and this is especially the case where the question in discussion depends upon the nature and force of general

principles. We would, however, earnestly request those who are disposed to entertain the objections above stated, to direct their serious attention and inquiries to the following points.

1. In a metallic currency, and where the law permits a free transport of the precious metals, the intrinsic value of the coin will of itself preserve the circulation at its proper amount: if it be too large proportionally to the circulation of other countries, a portion of the coin will pass through the exchanges abroad; if it be too small, the operation will be reversed; and thus in every transaction where commodities are exchanged for circulation, *i. e.* in every case of purchase or sale, an equivalent value is sure to be received.

2. In the case of a paper currency an attempt is made from considerations of convenience and economy to substitute paper notes in the place of metallic coins. In making this exchange we adopt a circulating medium which has no intrinsic value, and we therefore lose that self-acting security which we had with a metallic circulation, for the due regulation of its amount and the maintenance of its value. It therefore becomes necessary that we should resort to some artificial system or rule,

which shall secure with respect to a paper currency that regulation of its amount which in a metallic currency necessarily results from its intrinsic value.

3. Now a paper currency is nothing more than the substitution of paper notes in the place of what would otherwise be metallic coin, and the rule for the regulation of it seems to be very obvious, viz. that the paper notes ought to be kept the same in amount as the metallic coin would have been.

The amount of the import or the export of the precious metals is a pretty sure measure of what would have been the increase or decrease of the amount of a metallic currency.

Hence arises the obvious and unquestionable rule for the regulation of a paper currency, viz. that it should vary as a metallic circulation would have varied ; and the sure mode to accomplish this is to make the amount of notes out fluctuate in strict accordance with the import or export of the precious metals ; or, in the technical language of our present system, to make the circulation vary directly as the bullion.

4. Now all the objections above stated, and which we are now endeavouring to examine, rest upon the principle of wholly setting aside this rule; and if their validity be admitted, and the manage-

ment of the circulation be influenced by them, the consequence will be that the paper currency will not vary in amount, and therefore will not maintain the same value as the metallic currency for which it is intended to be merely a substitute.

5. But further than this—the amount of the paper currency upon the supposition now contemplated will be subjected to no fixed, definite, and understood rule whatever ; it will be left to vary according to the supposed wants of commerce ; and the nature of these wants and the extent to which they are to be met by a variation in the circulation, must be measured by individuals who will be left without rule or principle for their guidance, and who must therefore act under the influence of vague, accidental, and capricious impressions.

6. Let us here pause for a moment to reflect upon the consequence of leaving the circulating medium of a great country in this uncertain and lawless state.

In adopting a paper circulation we must unavoidably depend for a maintenance of its due value upon the adoption of a strict and judicious rule for the regulation of its amount. Upon such maintenance of its value depends the price of all

commodities; the relative situation of the debtor and creditor classes of the community. Every fluctuation in its amount directly affects the operations of trade, and may either tend to foster dangerous speculation or to cramp the energies of rising industry. Is it a matter of little moment to allow a machine of such mighty power to be released from the control of a principle acting constantly, certainly, and irresistibly? Is it wise or safe to leave its fearful oscillations to be regulated by the discretion of any individuals uncontrolled by fixed rule, and not made responsible for adherence to any recognised principle? What would be the condition of the material world were the great principles by which order is preserved amidst apparent irregularities to be suspended? At present we see the waves of the ocean swelling into fearful magnitude, and that vast body apparently preparing to break its bounds; but we know that an immutable law of nature has imposed certain limits to its action, and that its power of destruction is limited by a law which it cannot transgress. Let that law, however, be suspended; release the mighty monster for an hour from the influence by which its level is preserved, and the destruction of a world will be the immediate consequence.

The case under consideration is analogous to this. Fluctuations in a paper currency must, under the best system of regulation, occur to some extent, and be productive of occasional inconvenience ; but so long as the true principle of currency is maintained, we know that these fluctuations and their consequences are confined within certain and measured limits. The oscillations may for a period be even violent and mischievous ; but we know that they have their appointed bounds, and are subjected to a law which must ere long restore us to an equable and tranquil condition. But let that law be suspended ; leave the currency at liberty not merely to swell and roll on the surface, but wholly to break loose from the law which fixes its level, and what will be the consequence ? Confusion in all the transactions between man and man ; prices violently disturbed ; the mutual condition of different classes unjustly altered, and all the operations of trade subjected to convulsive agitations. And when this has once taken place, what will not be the difficulty of recovering our steps and retracing our path out of the pit into which we have descended ? To restore the ocean to its deserted bounds, and again subject its fluctua-

tions to a determinate law, will require the fiat of Almighty Power.

IX. Such are the consequences of yielding to mistaken views of present expediency, and abandoning for their sake the only true principle of currency. Let us bestow a moment's consideration upon the supposed evil of rigidly adhering to that principle.

All the inconveniences which are apprehended from an increase of the currency under the circumstances stated, may be reasonably apprehended in a still greater degree from the opposite course of permitting it to be contracted.

The steady influx of gold may be taken as a sure indication that the currency is deficient in amount, *i. e.* less in amount than it would be with a metallic currency; and therefore it is that the gold comes in. Was the currency metallic, this continuous influx of gold, by augmenting the circulation, would gradually remove the cause of, and therefore put a stop to, the influx. If, with a paper circulation, the notes be similarly increased as gold comes in, the effect will be the same; but if, as the gold comes in, the circulation be not increased, then the cause which produces the

influx is left in full operation, and gold may continue to come in to an unlimited amount. We may by this process arrive at a state in which the whole circulation will be represented by bullion in deposit, and thus the main object of a paper currency may be neutralised.

But under no management of the currency will matters be suffered to reach this point. At some stage in the progress, that step, which is improperly called a *forced* issue of notes, will certainly be resorted to; and in proportion as this step is delayed, will its effect, when resorted to, be found to be both sudden and violent: the effects urged as objections against the present adoption of the measure will all occur with increased intensity and suddenness. By a timely adherence to the rule contended for, these effects, which must occur to some extent, and would equally occur under a metallic currency, will, by their gradual introduction, be rendered moderate and comparatively insensible in their consequences. By thus acting we shall conform to that great rule of practical wisdom laid down by no less a man than Bacon, “Quidni tempus imitemur quod novationes ita insinuat ut sensus fallant,” and which is equally applicable to an action upon the

currency as to any other extensive or important change.

Every fluctuation in the amount of the currency necessarily brings with it inconvenience and disturbance in the operations of trade ; but the extent of this evil may be materially affected by the care which is taken to render those fluctuations gradual in their operation and limited in their extent. Any delay in commencing that change which an adherence to principle requires, whether it be a contraction of circulation in consequence of diminishing treasure, or an increase of circulation in consequence of an increasing store of bullion, will necessarily tend to render that action which must ultimately be resorted to more sudden when it occurs, and in all probability more extensive. By such temporary departure from the clear and distinct path which principle points out to her, the manager of the currency parts company from her sure and recognised guide, and enters into a region of obscurity, danger, and difficulty ; she subjects herself to a responsibility which she need not incur ; she endangers the foundation of our paper currency by suspending the principles on which alone it can rest ; and the very evil which she thus

endeavours to obviate will probably be augmented by the timid and reluctant manner in which she meets it.

In reply to this it may possibly be observed that the paper currency is convertible into gold, and that by any improper regulation of the amount of the paper money its value relatively to that of gold will be altered ; that the public will avail themselves of their power of converting it into gold, and thus rectify the evil.

It is undoubtedly true that convertibility is an ultimate security against a permanent *excess* of the currency, and fixes a limit beyond which such irregularity in its management cannot be carried. But this principle only comes into operation through the medium of prices. If the currency be in excess, prices of all articles are affected in a corresponding degree ; hence the balance of trade is disturbed ; the exchanges are consequently affected ; and a tendency is produced to export gold. Thus through the medium of convertibility the currency is restored to its proper amount. This result, however, will not be effected unless the rule be strictly adhered to of cancelling the notes in exchange for which the gold has been demanded. If this rule be neglected ; if the notes, as they are paid in for gold,

be re-issued through some other channel, and the circulation be kept up whilst the gold is exported, the principle of convertibility may continue in full action until the whole store of bullion is exhausted ; and thus the very foundation on which the paper currency rests will be shaken before the irregularity is corrected.

It thus appears that convertibility will not by itself prove a sufficient protection against excess in a paper currency. The rule which requires that the amount of the circulation shall be made to vary with the amount of the bullion is of essential importance ; and no system of paper currency can be secure which does not contain this as a self-rectifying principle. Convertibility should be looked to as an ultimate security ; but to render it such, and to regulate the frequency or violence of its action, a constant regard to the rule in question is requisite. The safety-valve is necessary as a precaution ; but its frequent or violent action would not be deemed the best evidence of the regular working of the engine ; that can only be secured by constant attention to the means by which the quantity or intensity of the steam is regulated : neither should we think it wise to rest the preservation of health upon the interposition of the physician, unaided by any

regard to the self-rectifying principle of daily regularity of life.

Against the opposite error, that of keeping the circulation too low, and not increasing the amount of notes in proportion to the influx of bullion, it is obvious that convertibility affords no security; and indeed, when principle is once departed from, it is difficult to say where the limit to that process is to be found, seeing, as we do by the accounts now before us, the amount of circulation diminished during a period in which the amount of bullion has doubled itself.

X. There is one other point involved in the objections which we are now examining, and which seems to require some remark. It is objected that the Bank, by increasing its issues, will lower the value of money, which, it is asserted, is already too cheap.

Two assumptions are involved in this objection. First, that the Bank, as regulator of the currency, does substantially possess the power of altering at her discretion the quantity of money and its value, *i. e.* the rate of interest; and, Secondly, that it is her duty to exercise that discretion, and in fact to regulate the amount of the circulation by reference to what she may deem to

be the proper state of money, or, in other words, the desirable rate of interest.

The power by this supposition vested in the Bank of England would indeed be formidable; the objections now urged against her monopoly, (as we think with no sufficient reason,) and the power which through it she obtains over the circulation, would in that case become irresistible. So long as she is bound down to a strict adherence to principle in regulating the currency, and is thus effectually precluded from an abuse of her power, her monopoly is beneficial to the public, and the only just objection to be urged against it is, that it is not more complete in its nature and its range more extended. But if she be permitted to exert her power with the view and for the express purpose of artificially affecting the state of money or the rate of interest, then indeed that power, being arbitrary and bound by no fixed rule, would be formidable and dangerous in the extreme, and the monopoly upon which it rests ought at once to be annihilated.

But it is clear that according to the true principles of currency the Regulator of the Circulation has no independent or discretionary power over the

state of money or the rate of interest. Her sole duty is to keep the circulation, in paper, what it would have been in gold ; her only function is to see that the fluctuations in the former correspond with accuracy to what would have been the fluctuations in the latter ; over these, either as to time or extent, she has no legitimate power whatever ; they are dependent upon those general circumstances which affect the operations of trade and the interchange of commodities between different nations. These are fortunately too various and powerful to be subject to the control of any private individuals or public body ; and the Bank, so long as she adheres to principle, is not justly obnoxious to any responsibility with respect to the state of money, or any consequences that may arise out of it. It is only when she quits her prescribed path, and assumes a discretion which does not properly attach to her, that she becomes justly subjected to such responsibility.

The impression, however, that the Bank does practically influence the abundance or scarcity of money and regulate the rate of interest is strongly impressed on the public mind ; and this effect is another of the many instances of confusion and error arising out of the mixed character of the Bank.

As a mere Regulator of the Currency she would keep out the requisite amount of notes, either by purchase of government securities, or by loans of money upon stated terms made to the highest bidder. Were she confined to transactions thus simple in their nature and steady in their action, there would be no confusion in the public mind as to the true nature of her duties, or the effect of her influence on the quantity or value of money. But in her capacity of Banker she undoubtedly possesses great positive resources as well as much moral influence, by the exertion of which she may and frequently does produce a strong effect upon the money-market. She cannot make any great movement in her banking capacity—such, for instance, as raising or lowering her rate of discount, or changing her investments, without producing a great sensation throughout all the minor bodies which revolve around her. These, not sufficiently analyzing the compound character of the Bank, and thus learning to distinguish the proper attributes of each function, are misled by their apparent identity, and attribute to the management of the currency that which is in fact the result of a simple banking operation on the part of a large and powerful body. We may perhaps render our

meaning more clear and intelligible by the aid of illustration. The sun is equally the centre to our system of light, and heat, and gravitation. But we should fall into strange confusion of ideas and some rather serious practical errors, were we to attribute the order of the planetary movements to the laws of heat, or to seek in the principles of gravitation the explanation of the optical phenomena around us. We fall into similar confusion of ideas, and of course are led to many practical errors, when, seeing that the Bank is at once Manager of the Currency and head of the banking operations of the country, we confound those distinct characters, and attribute power and effects to the former function which in reality are the result only of the latter.

XI. We have been tempted into a discussion of this branch of the subject under the impression that an important portion of the public are under the influence of erroneous views with respect to it. In the remarks which we have made, it has been our endeavour to point out those leading considerations from a due examination of which we think that a modification of their opinion may be reasonably anticipated. Fully to develop the grounds upon which those considerations rest, and

the consequences which they involve, would inevitably draw us into a more extended discussion than is consistent with the time at our disposal, and which would require abilities far greater than we can bring to bear upon it. Having alluded to the principles upon which it appears to us that the question ought to be decided, we must hope that those who feel the importance of the subject, or are excited by the interest of it, will undertake to examine those principles, and to trace out their consequences for themselves.

Such examination, we think, will lead them to two most important conclusions.

First. That the management of a paper-currency ought to be entrusted to one body only, invested with full power, and made exclusively responsible for the regulation of its amount.

Secondly. That such body ought to be restricted to the discharge of that one duty, and not be permitted to unite with it any other functions.

The issue of a paper-money being in fact the substitution of that which only represents value in the place of that which intrinsically possesses it, and that which is thus substituted being necessarily the common medium of exchange for the whole community, it seems preposterous to entrust a

power so delicate and obviously so capable of abuse, to more persons or bodies than are absolutely necessary for the accomplishment of the end in view.

For maintaining the value of the paper-money thus substituted for the precious metals, it is absolutely necessary that those who issue that money should regulate the amount of it by a steady and uncompromising adherence to a certain and defined rule. It seems obvious that the obligation to do this can be more effectually imposed upon one than upon a multiplicity of issuers.

The ordinary advantages to the community arising from competition are, that it tends to excite the ingenuity and exertion of the producers, and thus to secure to the public the best supply, due regard being had to the quality and quantity of the commodity, at the lowest price, whilst all the evils arising from errors or miscalculations on the part of the producers will fall upon themselves and not on the public. With respect to a paper-currency, however, the interest of the public is of a very different kind ; a steady and equitable regulation of its amount by a fixed rule is the end to be sought, and the evil consequence of any error or miscalcu-

lation upon this point falls in a much greater proportion upon the public than upon the issuers. To apply to a case of this nature the ordinary principle of competition seems strangely inconsistent and absurd.

These abstract considerations may be amply confirmed by practical experience. The effect of rival issues, not subjected to one controlling authority, in disturbing the monetary system of a country has been seen amongst ourselves during the last few years ; and a still more complete example of the principle of competition in full operation and producing all its legitimate fruits, is to be seen in the present state of the monetary system of the United States.

Upon the second point, the necessity of restricting the issuing body to that one duty alone, we need not repeat what we have so fully stated.

XII. We will now bring our observations to a close, lest we should wholly exhaust the patience of those who may be disposed to give these pages an attentive perusal, and add to the dryness of an abstruse and difficult subject by the tediousness of our commentaries.

We believe the circulation to be at this moment in an improper state.

We believe this state of the circulation and the difficulty in which the Bank is now placed to be the natural and perhaps inevitable result of her mixed character of banker and manager of the circulation.

We believe that the principal impediment to the adoption of that course which sound principle under existing circumstances would require arises out of the erroneous impressions and expectations entertained by the public with regard to the duties of the Bank.

And we believe that these erroneous impressions owe their principal strength and obstinacy to, if they do not altogether arise out of, the confused views of the principles of currency which are produced by the mixed character of the Bank.

If we are right in these opinions, we cannot doubt that according to the extent of our limited powers, we are rendering a useful service to the community by the attempt to invite public attention to a subject which so nearly concerns the pecuniary interest of every individual, as well as the permanent prosperity of the empire.

If we are wrong, most sincerely shall we welcome the correction of our error. To promote the removal of prejudices, and to assist in establishing in their place correct and sound views, is the only

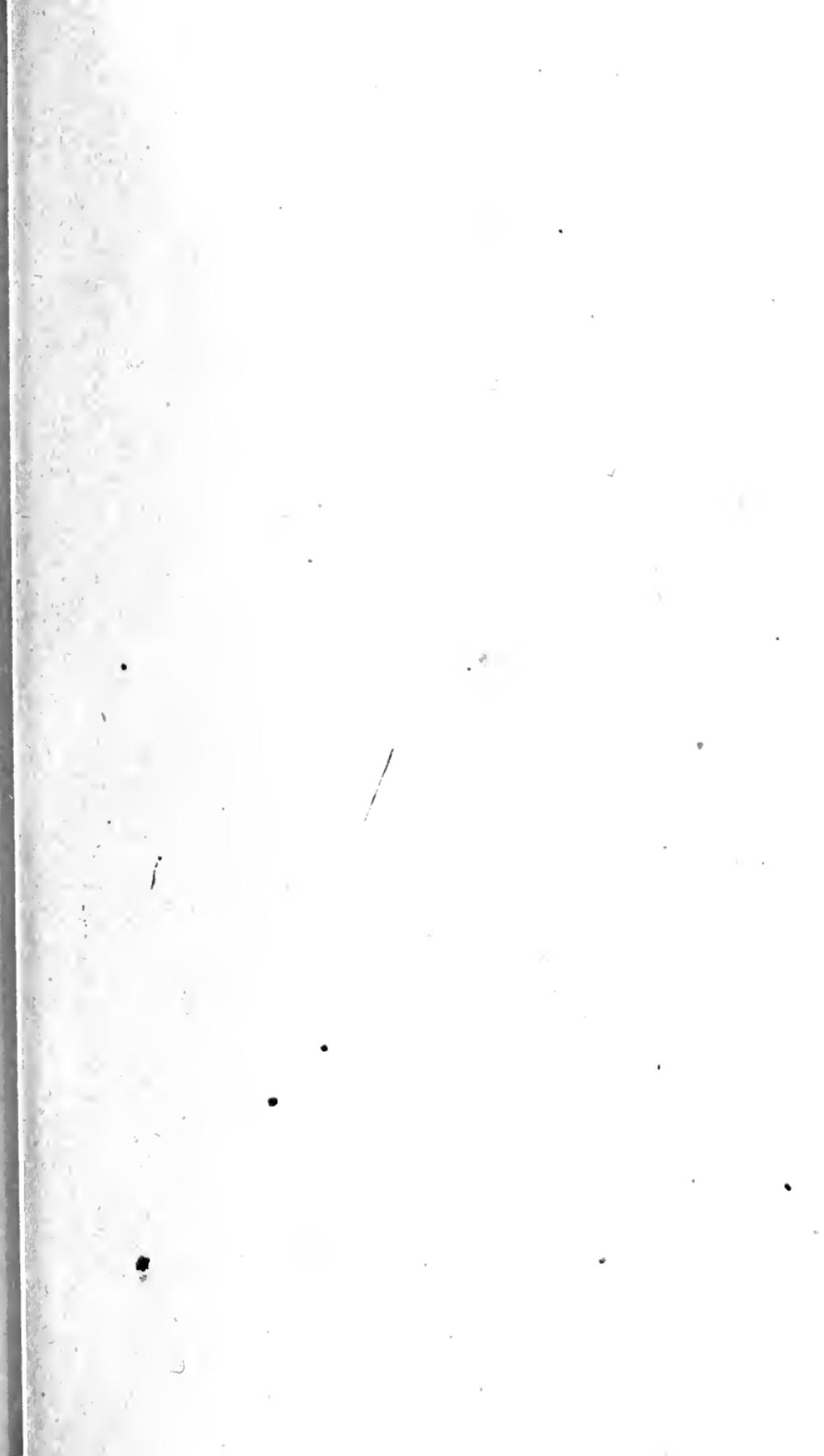
object at which we aim ; and for the attainment of this end we are anxious to fix the attention of the public on considerations which may otherwise escape their notice, and to induce them to hold under their steady contemplation, and to examine from different points of view, facts which are obvious to all. If by so doing we can advance our knowledge upon this subject one little step, or suggest a single hint which may be improved by abler heads, we shall not think that we have written in vain.

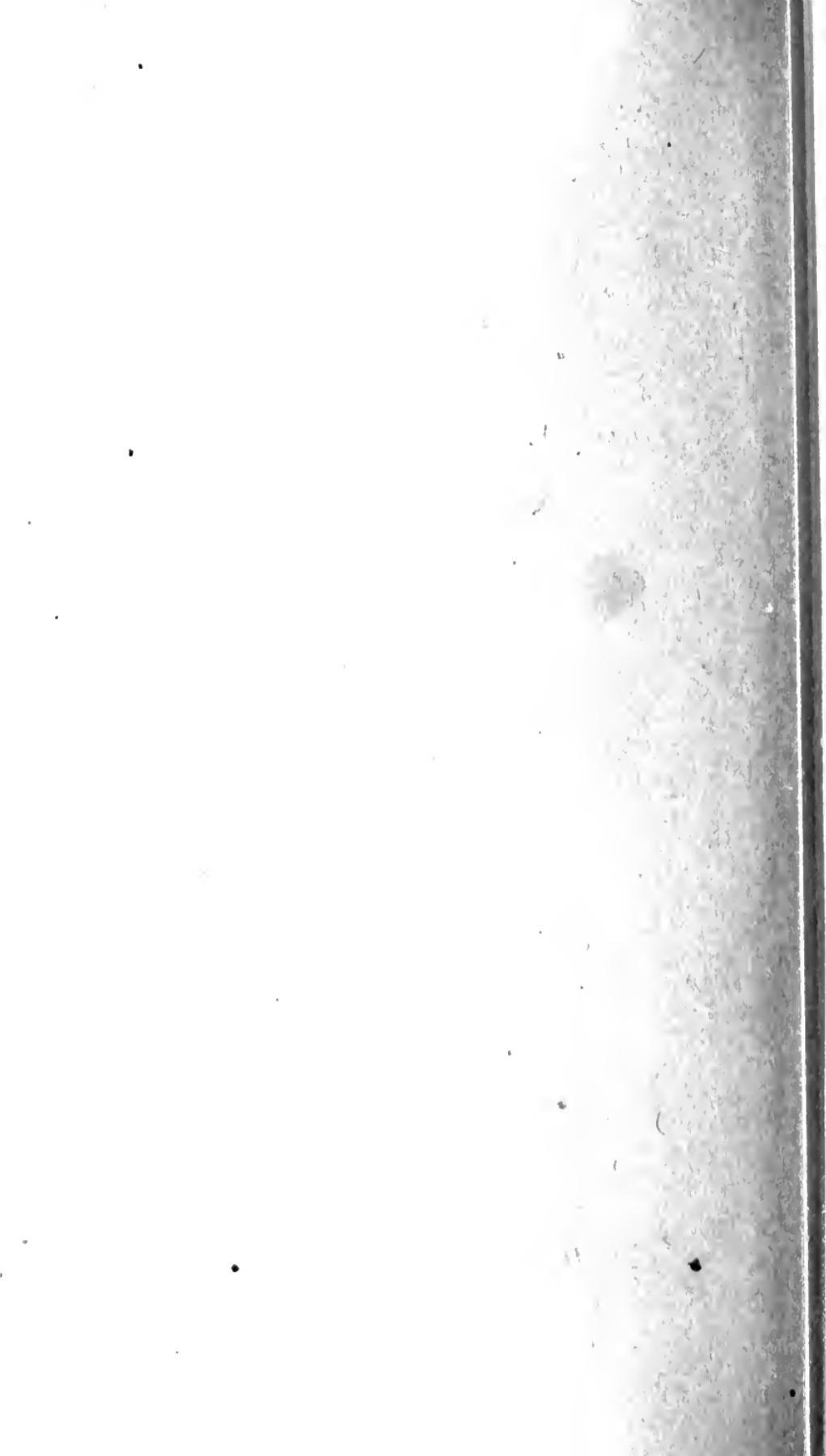
To you, kind reader, whose patience may have enabled you to keep company with us through this discussion, we cannot express our parting wish in language more concise or appropriate than that of the ancient poet,—

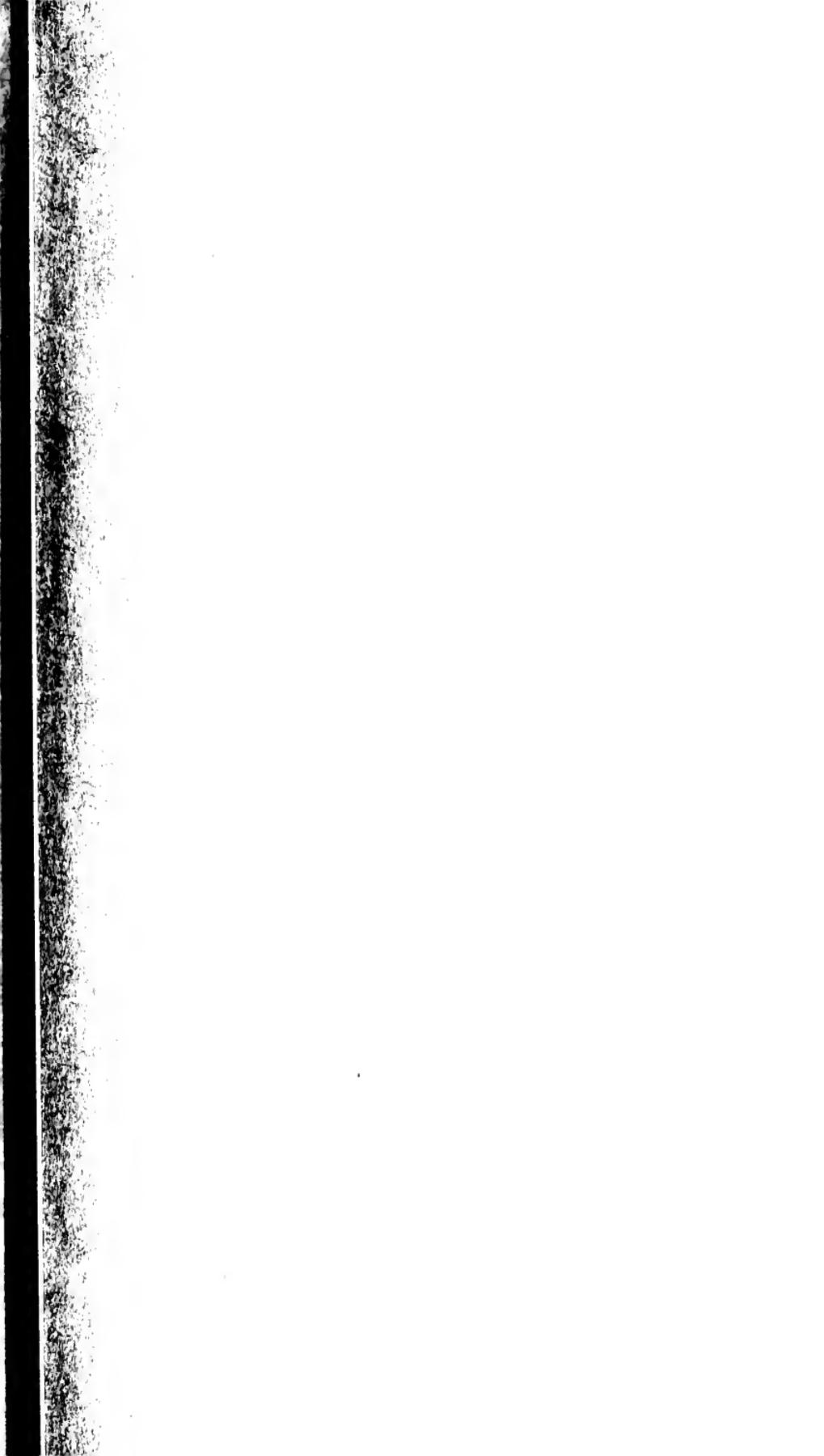
Si quid novisti rectius istis
Candidus imperti, si non his utere mecum.

London,
December 23, 1837.

THE END.







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